



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Number: 201012052
Release Date: 3/26/2010

Date: 2/11/2009

UIL Code: 513.00-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

M =

Dear :

This is in reply to your ruling request under section 513 of the Internal Revenue Code.

FACTS

You have been recognized as exempt from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3), and as a public charity described in section 509(a)(2). You contract with commercial employers and state and local government employers ("Employer Groups") to provide comprehensive, coordinated health care services for enrollees in a variety of prepaid healthcare plans operating in a number of states through a network of subordinate tax-exempt organizations (including several regional health plans) and non-exempt organizations.

One of your subordinates is M, a for-profit corporation that is licensed as an insurer in a number of states. You own 100 percent of M's preferred stock and 50 percent of M's voting common stock. Your affiliated medical groups own the other 50 percent of M's voting common stock.

You plan to establish an Administrative Services Only Program ("ASO Program") primarily for large, self-insured employers ("ASO Purchasers"). Under the ASO Program, ASO Purchasers will contract with M to receive certain administrative services, including claims adjudication, utilization management, disease management, quality assurance, eligibility and enrollment, and access to your integrated healthcare delivery system, including physicians, hospitals and other healthcare providers for covered employees (collectively, "ASO Services"). M will provide certain ASO Services by subcontracting with you and with your subordinate regional health plans. You will receive compensation from M on a capitated or other fair market value basis for providing these services. You represent that the amount of this compensation will be fair and reasonable in relation to the value of the services you will provide. You also represent that you

will spend only a very small percentage of your time on the provision of ASO Services to ASO Purchasers.

As part of your arrangements with Employer Groups, you provide various administrative services, not as separately identifiable services, but as necessary and integral parts of your overall arrangements with your Employer Groups. Similarly, under the ASO Program, through M, you will provide to ASO Purchasers as ASO Services the same types of administrative services. Under the ASO Program, M will not provide ASO Services to any ASO Purchasers that do not also include access to your integrated healthcare delivery system by their covered employees.

The healthcare providers to which ASO Purchasers' employees will have access generally will be the same as the healthcare providers to which your Employer Groups' enrollees have access. Under your arrangements with Employer Groups, in order to ensure access to emergency services and to infrequently required specialty services, Employer Groups' enrollees occasionally receive health care services from healthcare providers who are outside your integrated healthcare delivery system, but only on an episodic basis and in limited circumstances. Under the ASO Program, M will have the same arrangement with ASO Purchasers with respect to their covered employees. Therefore, under the ASO Program, through M, you will provide to ASO Purchasers as ASO Services the same types of related administrative services that you provide as part of your arrangements with Employer Groups.

RULING REQUESTED

Providing ASO Services in the manner described will not constitute an unrelated trade or business within the meaning of section 513 of the Code.

LAW

Section 501(a) of the Code states that an organization described in section 501(c)(3) is exempt from income taxation.

Section 501(c)(3) of the Code describes organizations organized and operated exclusively for charitable and other purposes.

Section 513(a) of the Code states that the term "unrelated trade or business" means any trade or business the conduct of which is not substantially related to the exercise or performance by such organization of its tax-exempt purpose.

Section 1.513-1(d)(1) of the regulations states that gross income derives from an unrelated trade or business, within the meaning of section 513(a) of the Code, if the conduct of the trade or business which produces the income is not substantially related to the purposes for which exemption is granted.

Section 1.513-1(d)(2) of the regulations states that a trade or business carried on by an organization is related to its tax-exempt purpose if the conduct of the business activities has a causal relationship to the achievement of the organization's tax-exempt purpose. It is "substantially related" if the causal relationship is a substantial one. Thus, the activity must contribute importantly to the accomplishment of the organization's tax-exempt purpose. Whether an activity contributes importantly to the accomplishment of the organization's tax-exempt purpose depends in each case upon the facts and circumstances involved.

Section 1.513-1(d)(3) of the regulations states that in determining whether activities contribute importantly to the accomplishment of an exempt purpose, the size and extent of the activities involved must be considered in relation to the nature and extent of the exempt function which they purport to serve.

ANALYSIS

Under the ASO Program, through M, you will provide to ASO Purchasers as ASO Services the same administrative services that you provide as part of your arrangements with Employer Groups. These administrative services are provided as necessary and integral parts of your overall arrangements with your Employer Groups. Thus, your provision of ASO Services to ASO Purchasers through M will be necessary and integral parts of you providing comprehensive, coordinated health care services for enrollees in a variety of prepaid healthcare plans, whether or not these administrative services are separately identifiable.

In addition, the size and extent of your ASO Services will not be disproportionately large in relation to the nature and extent of your tax-exempt purpose. See section 1.513-1(d)(3) of the regulations. Therefore, your provision of ASO Services will contribute importantly to the accomplishment of your tax-exempt purpose.

As a result, your provision of ASO Services will have a substantial causal relationship to the achievement of your tax-exempt purpose under section 1.513-1(d)(2) of the regulations. Consequently, your provision of these services will be substantially related to your tax-exempt purpose under section 1.513-1(d)(1), and will not constitute an unrelated trade or business within the meaning of section 513(a) of the Code.

RULING

Providing ASO Services in the manner described will not constitute an unrelated trade or business within the meaning of section 513 of the Code.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Steven Grodnitzky
Manager, Exempt Organizations
Technical Group 1

Enclosure
Notice 437